ECF Best Practices Open Forum Notes

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Lincoln, Nebraska

Chapter 13 Bankruptcy Best Practices
Hot Topics in Chapter 13
Kathleen Laughlin, Chapter 13 Trustee

1. Welcome and Introduction by Kathleen Laughlin.

a. Kathleen Laughlin - Chapter 13 Trustee
b. Marilyn Abbott - Attorney
c. Tom Kenny - Attorney
d. Kathy Adams - Staff
e. Debby Valenti - Staff

2. Purpose of the Chapter 13 Best Practices Forum.

The Chapter 13 Trustee, will review recent decisions dealing with Chapter 13 and consumer bankruptcy issues and discuss practice tips and due diligence for handling consummer bankruptcy cases.

3. Sixty Month Plan Required for Above Median Income Debtors in the 8th Circuit.

a. On October 27, 2008, **Coop v. Frederickson** - F.3d -, 2008 WL 4693132, C.A.8, October 27, 2008 (NO.07-3391) was decided by the Eighth Circuit Court of Appeals, adding its voice of the national confusion over the required length of chapter 13 payment plans. The Court of Appeals ruled that for a chapter 13 debtor whose income was above the median, but whose form B-22C disposable income was negative, the debtor was required to propose either a full payment plan, or a sixty month plan which paid creditors claims in full or in part. The court therefore disagreed with the Nineth Circuit Court of Appeals' decision in Maney v. Kagenveama, which allowed an over-median but negative B-22C debtor to propose a partial payment plan of 36 months duration. This decision comes more than a year after the 8th Circuit Bankruptcy Appellate Panel concluded the exact opposite.

b. In **Coop**, the appeals court also held that despite the presence of a negative disposable income figure on Form B-22C, if the debtor's Schedules I and J revealed a positive disposable income figure, the debtor may be obligated to pay that disposable income figure into the plan. This ruling effectively emasculates form B-22C, rendering it superfluous if the logic of this case is followed to its conclusion. In the words of the court, Form B-22C is a "starting point" for determining the bankruptcy debtor's disposable income to be devoted to making chapter 13 plan payments. However, from

this starting point, the court is required to consider changes in the debtor's situation, and also the debtor's actual income and expenses.

c. This approach contemplates that the debtor's actual income and expenses, as reported on Schedules I and J, will be used to determine the final chapter 13 plan payments. The court's ruling in **Coop v. Frederickson** resurrects Schedules I and J, placing it ahead of Form B-22C in importance. It re-introduces the view that the debtor's actual ability to pay dictates the amount of the plan payment, and it requires 60 month plans for all above-median chapter 13 debtors.

Question: What about plans that are already confirmed?
Answer: We will not go back and check those cases.

Question: So, do we keep COOP in mind when revising a plan?
Answer: Yes, keep COOP in mind when revising plan.

4. Best Practice for Determining Projected Disposable Income.

a. Compare B22C and Schedule I & J and select the method that most accurately reflected the debtor's post-petition ability to pay unsecured creditors.

1. **In Re Hardacre**, 338 B.R. 718 (Bankr. N.D. Texas 2006)
2. **In Re Jass**, 340 B.R. 411 (Bankr. D. Utah 2006)
3. **In Re Kibbe**, 2006 WL 1300993 (Bankr. D.N.H.)
4. **In Re Schanuth**, 342 B.R. 601 (Bankr. W.D. Missouri 2006)
5. **In Re McGuire**, 2006 WL 1527146 (Bankr. W.D. Missouri 2006)
6. **In Re Clemons**, No. 05-85163 (Bankr. N.D. Georgia June 2006)
7. **In Re Dew**, No. 06-40154-JJR-13, 2006 WL 1691130 (Bankr. N.D. Alabama June 21, 2006)
8. **In Re Grady**, No. 06-20104, 2006 WL 1689324 (Bankr. N.D. Georgia June 21, 2006)
9. **In Re Wilbur**, No. 06-20104, 2006 WL 1687586 (Bankr. D. Utah June 21, 2006)
10. **In Re Fuger**, No. 06-20801, 2006 WL 1777341 (Bankr. D. Utah June 29, 2006)
11. **Coop v. Frederickman**, - E3d - , 2008 WL 4693132, CA 8, October 27, 2008 (No. 07-3391)

*These two cases listed below were omitted from Kathy's original list above, but mention during her breakout session.

1. **Hamilton v. Lanning** - 10th Circuit case - November 13, 2008
2. **Hilderbrand v. Petre** - 6th Circuit Appellent case

5. Best practice for Completing Form B22C.

1. Debtor's counsel needs six (6) months of paystubs and tax returns to prepare filings for bankruptcy. Trustee will object if these are not provided to her office so just pro-

vide them in advance.

*Kathleen Laughlin - Stresses how important it is that these items are provided to her in advance.

2. Provide the Trustee with the remaining balances of any 401k loans.
3. For Line 57 - Deduction for Special Circumstances - debtor's counsel must provide the Trustee with documentation and detailed explanations for "special circumstances."
4. Debtor's B22C form and the Schedules I and J should not be significantly different or a Trustee's objection may be filed.

6. Best Practice for Adequate Protection Orders.

a. Recently there has been a major increase in the number of adequate protections motions filed by a major retail creditor. These motions have asked for a minimum payment of $100 to a maximum payment of $225 per month.

b. Several objections to these motions have been filed by debtor's attorneys and these motions and objections are pending before the Court. Be alert for upcoming decisions on these motions and objections.

c. Any plan filed after the approval of an adequate protection motion or stipulation should contain provisions consistent with the motion or stipulation. Plan provisions should not conflict with the prior adequate protection orders or create funding problems. If the plan does not reflect the terms of the approved motion or stipulation, this will likely cause an automatic ambiguity in the plan which may lead to objections by a creditor or the Trustee.

*Kathleen Laughlin - Make sure orders and or stipulations are carefully reviewed. Language from order or stipulation should go into amended plan.

7. Best Practice for Stripping Wholly Unsecured Junior Mortgage.

A. Concept of Mortgage Stripping

1. A cardinal rule of bankruptcy has been and continues to be that first mortgage on primary residences are specially protected from modification in bankruptcy.
    a) Hence, when the value of a home decreases below the value of a first mortgage, a debtor has no ability to modify the debt in bankruptcy and keep his home.
    b) Statutory authority: 11 U.S.C. 1322(b)(2) Contents of plan... "Subject to subsections (a) and (c) of this section, the plan may -

        (2) modify the rights of holders of secured claims, other than a claim secured only be a security interest in real property that is the debtor's principal residence, ..."

c) Indeed, this is one of the topics that Congress debated during the recent TARP "Troubled Assets Relief Program"/bailout legislation, but no change were made to the existing law.
"Subject to subsections (a) and (c) of this section, the plan may -

(2) modify the rights of holder of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence,..."

2. The same anti-modification rule does not apply to mortgages on properties that are not used as one's primary residence or to second, third, and even more junior mortgages if they are "wholly unsecured" - even if they are secured by a primary residence.
    a) A debt is wholly unsecured if no part of the value of the collateral secures it.
    b) This is easier explained with examples.
    c) Example of "wholly unsecured:" if the home is worth $200,000, and the first mortgage payoff is $205,000 and the second mortgage payoff is $50,000, then then the second mortgage is wholly unsecured because none of the value of the collateral secures it.
    d) Example of "not wholly unsecured:" if the home is worth $200,000, and the first mortgage payoff is $190,000, and the second mortgage payoff is $50,000, the second mortgage is not wholly unsecured because $10,000 of the value of the collateral secures it.

B. Why Do it?

1. Wholly unsecured junior mortgages are more and more common now as real estate values decrease.

2. If a Chapter 13 debtor has a wholly unsecured junior mortgage, he can discharge it in a Chapter 13 bankruptcy and keep his home.
    a) Note: this option is not available in a Chapter 7 bankruptcy.
    b) This can result in a huge financial benefit for a homeowner, especially one struggling to keep up with multiple mortgages.
    c) If this situation applies to one of your clients, you are faced with a decision as to what is the best practice for stripping such a lien.

C. How to Strip the Mortgage Effectively

1. The best method would be to file an adversary proceeding pursuant to Federal Rule 7001(2) and request the United States Bankruptcy Court to determine the validity, priority, or extent of a lien or other interest in property.
    a) Avoiding liens in bankruptcy can sometimes be confusing because some can be avoided by motion.
    b) Consider that filing a motion to avoid lien may result in a "text only" order.

Then how do you legally enforce that "text only" journal entry in a real estate transaction?

c) Moreover, the Federal Rules proscribe which actions must be done by adversary proceedings. Since stripping wholly unsecured junior mortgage falls directly within the language of FR 7001(2), it would appear that the federal rule should be followed.

d) Consider also that the successful outcome of the adversary proceeding will result in a legally enforceable judgment that can be transcribed at the Register of Deeds office after the debtor has successfully received a discharge in Chapter 13.

e) At present the debtor does not have to pay a filing fee to file an adversary proceeding so that is also a "plus" factor for your consideration.

f) Bear in mind that the issue is the value of the property at the time the case is filed. Don't wait 3 or 4 years into the plan to get an appraisal of the property.

D. Recent Nebraska Cases On This Issue

1. Successful Stripping Obtained by Adversary Proceeding Pursuant to FR 7001(2) in 2 cases where U.S. Bankruptcy Judge Timothy J. Mahoney presided: See

   a) Bostwick v. US Bank, Bk. No. 08-81702, Adv. No. 08-8046 (Bankr. D. Neb. November 6, 2008)

   b) Alsman v. Home comings Financial, Bk. No. 08-81534, Adv. No. 08-8040 (Bankr. D. Neb. November 6, 2008)

2. Unsuccessful Stripping Obtained by Adversary Proceeding Pursuant to FR 7001(2) in 1 case where Chief, U.S. Bankruptcy Judge Thomas L. Saladino presided: See

   a) Hoesing v. Countrywide Home Leading, Bk. No. 08-81219, Adv. No. 08-8034 (Bankr. D. Neb. November 6, 2008)

In **Hoesing v. Countrywide Home Leading**, Bk. No. 08-81219, Adv. No. 08-8034 (Bankr. D. Neb. November 6, 2008) Chief Judge Saladino denied the debtor/plaintiff's motion for summary judgment.

- Here the same attorney served at a post office box the Defendant corporation only (not an officer, a managing or general agent, or any other agent authorized to receive service of process) as required by FRCP 4.

- The Court also opined that the Plaintiff was seeking a motion for default judgment since the Defendant had not responded. However, even if the Plaintiff was seeking a motion for summary judgment, the Court was concerned about a lack of foundational affidavit And compliance with Neb. R. Bankr. P. 7056-1.

8. Best Practice to Appeal Objection to Confirmation

Zahn v. Fink, 526 F. 3d 1140 (8th Cir. 2008).

Appellant Zahn filed a bankruptcy petition under Chapter 13. Her petition did not include the distributions her non-filing husband received from an IRA account. The Chapter 13 Trustee, appellee Fink, objected to the confirmation of the plan, and Zahn was required to include the IRA income. She then objected to her own plan, which was eventually confirmed. She appealed confirmation of the plan to the Bankruptcy Appellate Panel (BAP), which dismissed the appeal for lack of standing. Zahn appealed the BAP's finding, and the 8th Circuit Court of Appeals reversed the BAP.

1. The bankruptcy court's interpretation of the law is reviewed de novo and its findings of fact for clear error.
2. In order to have standing to appeal the decision of the bankruptcy court, an appellant must be a person aggrieved.
3. Generally, a party may appeal from a judgment in his favor when there has been some error prejudicial to him, or he has not received all he is entitled to.
4. The extended length of Zahn's plan, caused by including the disputed income, is material and prejudicial to her, and she is therefore an aggrieved party.
5. Confirmation of a plan generally acts as a final order and the appellate court has jurisdiction over final orders. An order denying confirmation of a plan, which does not dismiss the case, is not a final order and cannot be appealed.
6. Confirmation of Zahn's plan is a final order and is appealable.
7. Not allowing a debtor to appeal confirmation of her own plan would require a debtor to comply with a plan that contains provisions the debtor does not believe are required by the Bankruptcy Code, while losing her right to appeal those provisions.
8. The 8th Circuit of Appeal held that a debtor who objects to her own plan may be an aggrieved party and have standing to appeal confirmation of such plan.

9. IRA Withdrawals Are Not "Income" in Bankruptcy

In Zahn v. Fink, (06-6072, August 14, 2008). Withdrawals from retirement accounts do not count as "income" for the bankruptcy means test, according to the Eight Circuit Bankruptcy Appellate Panel.

- The BAP has not held that such withdrawals, although potentially taxed as income by the Internal Revenue Service, are not "income" to the debtor when taken because they are in fact simply the liquidation of an existing asset. In effect, it is no different than a withdrawal from a bank account - taking money from one pocket and moving it to the other. The "income" event was when the money first became available to the individual from wages or the tooth fairy. But once the consumer directed it to be deposited into a retirement plan, the debtor did not lose the asset, but merely gained a possible tax advantage (as well as safe-keeping from creditors, typically).

- The BAP also pointed out that the result is more in line with the purpose of the means Test: To identify consumers who do in fact have regular income sufficient to make a

meaningful repayment of unsecured debt. Unless the consumer has a bottom-less pit of retirement funds, it is unreasonable to expect that withdrawals could or would continue for a full five-year period to assist in performing a repayment plan.

10. Reporting of Social Security Numbers

1. Some Chapter 13 debtors are employed by federal agencies who have informed the Chapter 13 Trustee that they will not set up or release employer withholding unless they are furnished with a full social security number.

2. The Chapter 13 Trustee will not provide this information to a third party.

3. Thus, in order to insure that the withholding begins or ends, we are sending letters to debtor's counsel and asking that debtors' counsel send a copy of the Court's Order to the federal agency at the address listed on the bottom of the Court's Order and include the debtor's full social security number at the top of the order.